

# [Fin 352](https://assignbuster.com/fin-352/)

[Finance](https://assignbuster.com/essay-subjects/finance/)

Finance Questions Buckets are a group of securities having similar risk levels. The general idea behind re-pricing is based on profit maximization by adapting to the changing economic situations and due to variation of terms by regulatory bodies.
Duration is the value-weighted measure of a security’s maturity or other assets that are income generating. It considers the timing and the amount of the possible cash flows from the assets.
Studying duration is important as it enables one determine how well the timings of cash outflows match those of cash inflows.
Duration is applied by finding the mean of the duration under simulation models of various interest rates possibilities in the future.
The duration gap for a financial institution is a way given as the duration of the earning assets less the product of the duration of the paying liabilities and the quotient of paying liabilities and earning assets.
Value at Risk (VAR) is a measure of the potential value loss that a risky portfolio or asset is exposed to over a certain time period for a specific confidence interval. It shows possible value loss from “ normal market risk” and not from all risk, with proper distinction between abnormal and normal risk and between non-market and market risks.
VAR does not fully relate to the normal distribution as it is determined only up to a certain level to the left of the distribution curve.
VAR can handle extreme events to a certain degree effectively given the confidence level is properly chosen.
VAR can be applied to portfolios by calculating the possible risk considering the total market and nonmarket risks within a certain confidence level then getting the risk factor over time.
Securitization is the pooling of various contractual debt types like commercial and residential mortgages and selling them in consolidation to various investors as pass-through securities, bonds or as collateralized mortgage obligation.
Benefits of securitization:
Receivables are taken “ off balance sheet” then replaced with equivalents in cash. This improves an originator’s balance sheet, securitization can thus enhance the managerial control over structure and size of a company’s balance sheet.
With securitization, there is more efficient private sector institution financing as an organization’s weighted-average capital cost is lowered.
The originators do not need to wait till receiving receivables’ payment to get funds to run their businesses and generate more receivables.
Since the originator acts as a servicer and there is no need to notify obligators under receivables, to the originator’s customers the transactions are transparent.
In non-revolving structures, together with those having receivables at fixed interest rates, assets and liabilities marching can be done, this eliminates need for hedging.
Problems involved in Securitization:
Synchronization of interest generated from the pool and interest paid to investors involves a tedious and arduous process.
Highly sophisticated documentation is required which should cover all potential risks due to the complexity of transaction. As a result, a lot of time is consumed.
Mortgage transfers are difficult for legal, tax or regulatory reasons as they need to comply with requirements set by regulatory authorities.
Tranches refer to portions of a deal, which is one of a number of related securities offered at a go but having different risks and maturities or rewards.
Financial leverage refers to the techniques used to multiply either gains or losses. Many times it involves buying a lot of assets using borrowed funds in anticipation that the appreciation will be higher than the borrowing cost.
In futures markets, leverage is having control over huge cash amounts for commodities that have comparatively small capital levels. In futures markets, price leveraging is common resulting in small changes in futures prices translating into huge gains or losses.
Futures margin is the cash amount an investor has to put up in order to open a trading account.
Maintenance margin is the minimal amount future traders are required to maintain in their margin accounts for them to hold future positions.